

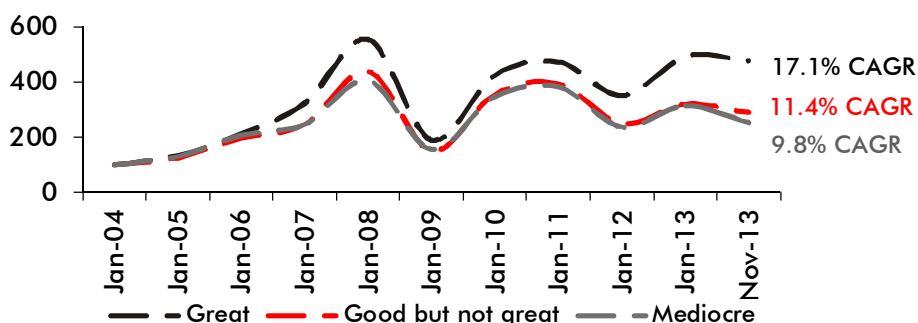
Ten baggers 3.0

Over the past two years, we have used our 'greatness' framework to identify structurally strong businesses in India. These companies were identified based on their relentless improvement in financial performance over long periods of time (usually, six years). Using FY13 annual reports, we now refresh our list of ten baggers. The first two iterations have cumulatively delivered 31% (over the past two years) on an absolute basis and 10% relative to the BSE500.

Structural plays, beyond cyclical worries

Whilst 'Good & Clean' remains our preferred tactical way of playing Indian equities, we cannot lose sight of the big picture in a country like India where the robustness of the economy ensures that well-managed companies focused on cash generation have a high chance of doing well. Structural plays, like the ones we aim to identify here, are financially strong firms (with credible management teams) that remain consistent performers on a cross-cyclical basis. Both in live portfolios and back-tests, the approach delivers alpha in most years.

Last ten years' back-test on the 'greatness' framework



Source: Ambit Capital research

The 'greatness' philosophy

Consistent improvements in corporate performance are more important than 'great leaps'—this has been the guiding philosophy of our 'greatness' framework which lies at the core of our process of identifying structurally sound businesses. Not only do the great firms perform significantly better than an average firm on a variety of measures, more importantly, they show a more consistent and calibrated approach to growth over long periods. In this note, we update our 'greatness' framework to include FY13 numbers.

The framework uses the following attributes to measure consistent financial improvements: judicious capex, conversion of capex to sales, pricing discipline, balance sheet discipline, cash generation and net profit improvement, and return ratio improvement.

The winning stocks

We find that 77 firms from the BSE500 pass more than two-thirds of the tests in our greatness framework. Of these, the best 30 firms that clear our accounting quality and corporate governance filters make it to this year's list. Of these 30 firms, we have bottom-up coverage with BUYs on: Cummins India, Supreme Industries, TTK Prestige, Eicher Motors, Torrent Power, Persistent Systems, eClerx Services, Tata Motors and Bajaj Auto.

Exhibit A: The 'ten baggers'

Ticker	Company	Mcap (US\$ mn)
Attractive valuations*		
BJAUT IN	Bajaj Auto	8,868
CDH IN	Cadila Health	2,447
KKC IN	Cummins India	1,891
DBCL IN	DB Corp	771
MCLR IN	McLeod Russel	491
SHOP IN	Shoppers Stop	438
TTMT IN	Tata Motors	17,974
TPW IN	Torrent Power	770
Moderate valuations**		
BYRCS IN	Bayer Crop Sci.	1,019
BOS IN	Bosch	4,300
CU IN	Carborundum Uni.	351
ITC IN	ITC	39,888
KSCL IN	Kaveri Seed Co.	349
LPC IN	Lupin	6,078
MRF IN	MRF	1,153
TTKPT IN	TTK Prestige	609
Rich valuations***		
APNT IN	Asian Paints	7,925
BATA IN	Bata India	1,087
CSTRL IN	Castrol India	2,289
ECLX IN	eClerx Services	536
EIM IN	Eicher Motors	1,829
SKB IN	GlaxoSmith C H L	2,958
IPCA IN	Ipca Labs.	1,379
KJC IN	Kajaria Ceramics	294
PI IN	PI Inds.	485
PAG IN	Page Industries	875
PSYS IN	Persistent Systems	567
SI IN	Supreme Inds.	798
TRP IN	Torrent Pharma	1,237
VST IN	VST Inds.	390

Source: Ambit Capital research

* Trading below five-year P/E, P/B, EV/EBITDA (on at least two of these three measures)

** Trading below either five-year P/E, five-year P/B or five-year EV/EBITDA (on one of these three measures)

*** Trading above five-year P/E, P/B, EV/EBITDA

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Philosophy and framework

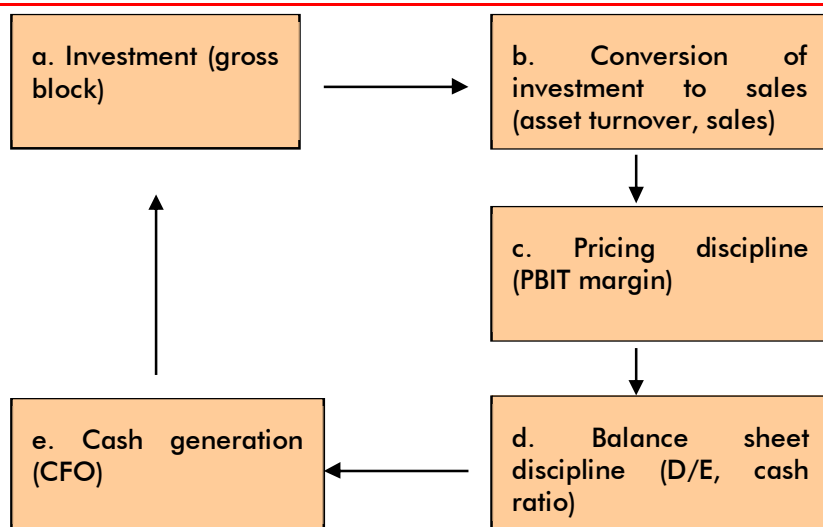
“Greatness is not in where we stand, but in what direction we are moving....”

- Oliver Wendell Holmes

This quote appropriately captures the driving philosophy behind our ‘greatness’ framework that lies at the core of our process of identifying potential ten baggers. We had unveiled this framework on 19 January 2012 with the first iteration of the ‘Tomorrow’s ten baggers’ note. This framework studies a firm’s structural strengths by focusing not on absolutes but rather on improvements over a period of time and the consistency of those improvements.

A basic sketch of the underlying process behind the making of a great firm has been recaptured in Exhibit 1 below.

Exhibit 1: The ‘greatness’ framework



Source: Ambit Capital research

We rank the BSE500 universe of firms (excluding financial services firms and excluding firms with insufficient data) on our ‘greatness’ score, which consists of six equally weighted headings—investments, conversion to sales, pricing discipline, balance sheet discipline, cash generation and EPS improvement, and return ratio improvement.

Under each of these six headings, we further look at two kinds of improvements:

- **Percentage improvements in performance** over FY11-13 vs FY08-10; and
- **Consistency in performance** over FY08-13 i.e. improvements adjusted for underlying volatility in financial data

A complete list of factors that are considered whilst quantifying greatness has been provided in Exhibit 2 on the next page.

The ‘greatness’ framework

The framework essentially hinges on using publicly available historical data to assess which firms have, over a sustained period of time (FY08-13), been able to relentlessly and consistently:

- (a) Invest capital;
- (b) Turn investment into sales;
- (c) Turn sales into profit;
- (d) Turn profit into balance sheet strength;
- (e) Turn all of that into free cash flow; and
- (f) Invest free cash flows again.

Clearly, this approach will have limited value if there is a structural break in the sector or in the company, which makes past performance a meaningless guide to future performance. (For identifying structural breaks of this sort, for example in the Indian boiler-turbine-generator sector or in the Indian utilities sector, we look to our sector leads for help.)

However, to the extent that such structural breaks tend to be the exception than the rule, the greatness model helps in creating a shortlist of stocks that investors can then analyse in greater detail.

Put simply, the greatness model separates the wheat from the chaff. Yet, it does not cook the whole meal for you!

Exhibit 2: Factors used for quantifying greatness

Head	Criteria
1 Investments	a. Above median gross block increase (FY11-13 over FY08-10)*
	b. Above median gross block increase to standard deviation
2 Conversion to sales	a. Improvement in asset turnover (FY11-13 over FY08-10)*
	b. Positive improvement in asset turnover adjusted for standard deviation
	c. Above median sales increase (FY11-13 over FY08-10)*
	d. Above median sales increase to standard deviation
3 Pricing discipline	a. Above median PBIT margin increase (FY11-13 over FY08-10)*
	b. Above median PBIT margin increase to standard deviation
4 Balance sheet discipline	a. Below median debt-equity decline (FY11-13 over FY08-10)*
	b. Below median debt-equity decline to standard deviation
	c. Above median cash ratio increase (FY11-13 over FY08-10)*
	d. Above median cash ratio increase to standard deviation
5 Cash generation and PAT improvement	a. Above median CFO increase (FY11-13 over FY08-10)*
	b. Above median CFO increase to standard deviation
	c. Above median adj. PAT increase (FY11-13 over FY08-10)*
	d. Above median adj. PAT increase to standard deviation
6 Return ratio improvement	a. Improvement in RoE (FY11-13 over FY08-10)*
	b. Positive improvement in RoE adjusted for standard deviation
	c. Improvement in RoCE (FY11-13 over FY08-10)*
	d. Positive improvement in RoCE adjusted for standard deviation

Both improvement and the consistency of those improvements are important

Source: Ambit Capital research. Note: * Rather than comparing one annual endpoint to another annual endpoint (say, FY08 to FY13), we prefer to average the data out over FY08-10 and compare that to the averaged data from FY11-13. This gives a more consistent picture of performance (as opposed to simply comparing FY08 to FY13).

We rank the BSE500 universe of firms (excluding financial services firms) on this score to arrive at this year's rankings on this measure of structural strength. After removing financial services firms and firms with insufficient data, 380 firms from the BSE500 were ranked based on this measure. The highlights from the distribution of these firms on our 'greatness' score are displayed on the next page.

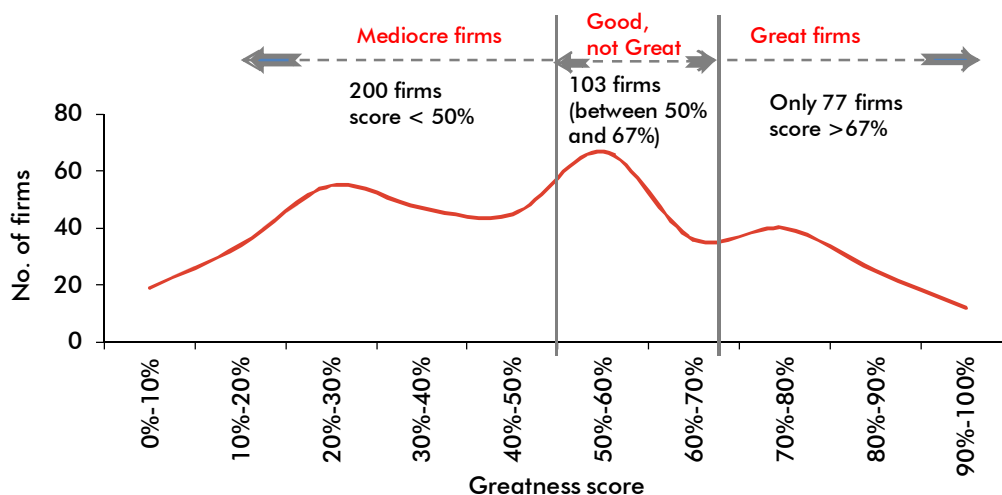
On page 6, we show a ten-year back-test of this framework and find that it does work. On pages 12-13, we show the real world performance of these sets of portfolios over the last year and demonstrate that the construct works in the real world. The lists from the BSE500 universe have delivered 31% on an absolute basis and 10% on a relative basis over the last two years. The list from the sub-BSE500 universe that we had published in January 2013 has delivered 22% in absolute terms and outperformed the BSE Smallcap Index by 41% over the year.

On pages 7-10, we delve into this year's list of 30 firms that constitute ten baggers 3.0. This is followed by a list of 16 firms from the sub-BSE500 universe that does well on the framework.

Quantifying greatness

From the universe of BSE500 firms, after removing financial services firms and firms with insufficient data, 380 firms were scored on the six headings highlighted on the previous page. The cut-off for greatness was placed at **67%*** and only 77 firms (20% of the total population of 380 firms) could manage a score above this cut-off.

Exhibit 3: Distribution of firms on the greatness score (total population: 380 firms)



Source: Ambit Capital research

In the next exhibit, we present key financial data on the three zones defined above: Mediocrity (200 firms), Good but not great (103 firms), and Great (77 firms).

Exhibit 4: Zones of greatness - Financial summary

	Mediocre	Good but not great	Great
Number of firms	200	103	77
Mcap (US\$ mn)	345	356	798
Share price (3-year CAGR)	-17%	1%	7%
Gross block (3-year CAGR)	14%	18%	17%
Sales (3-year CAGR)	15%	20%	20%
Adj PAT (3-year CAGR)	-4%	18%	25%
CFO (3-year CAGR)	2%	14%	12%
PBIT Margin (3-year average)	11%	13%	15%
RoE (3-year average)	11%	19%	23%
RoCE (3-year average)	12%	21%	24%
Net debt equity	0.6	0.2	0.2
Trailing 12 month P/E	14.3	15.6	17.9
Trailing 12 month P/B	1.2	2.4	3.6
Trailing 12 month EV/EBITDA	9.4	9.9	11.0

Source: Capitaline, Ambit Capital research; Note: All figures are based on median values of the firms analysed.

With regard to fundamentals, the superiority of the great firms compared with the other two groups is evident in Exhibit 5. However, what is interesting to note is that since we started with this exercise two years ago, we have seen the median market cap differential between the Great and the other two buckets widen, suggesting that the continuing downturn has proved much more brutal for the smaller caps.

Of these 77 great firms, we identify the ones that perform the best on our accounting and corporate governance filters, and this leads to our final list of 30 great companies. We present these 30 potential ten baggers in the next section.

*The greatness score is calculated by assigning equal weightages to the six factors outlined in Exhibit 2 on page 4.

Thus, each of these six factors carries a weightage of 16.7%. The scoring on sub-criteria within each of these factors is binary, with a firm getting either 1 or 0 based on whether it has done better than the respective threshold or not.

These scores are then cumulated to arrive at a final greatness score on 100 for the firm.

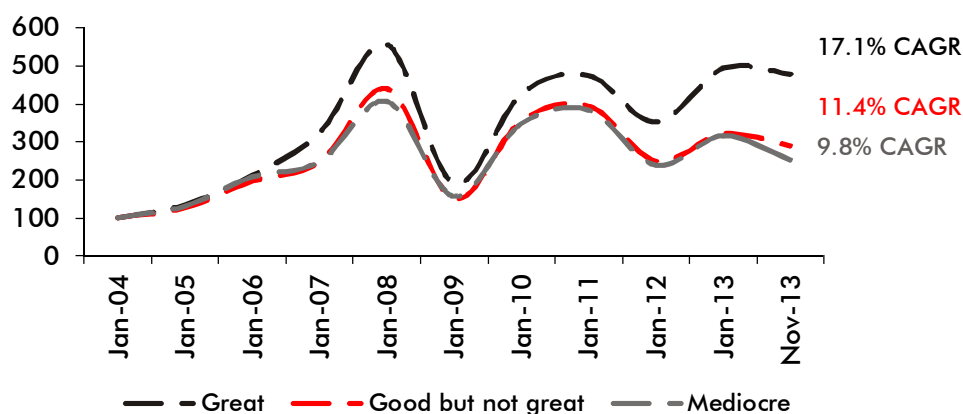
Does this approach work?

The 'greatness' approach has served us well in live portfolios, both in the ten-baggers format and as a tool for stock selection in the Good & Clean portfolios. That this approach works on a cross-cyclical basis is supported by a back-test of the framework.

Our back-test of the 'greatness' framework in India, going back to 2003 (which implies using data since 1997-98), shows that the 'great' firms deliver superior results; they outperform their 'non-great' peers by 6.5% on an average CAGR basis respectively (over a ten-year period from 2004-2013).

'Great' firms are firms that score more than 67% on our framework, 'good' firms score between 50% and 67% whilst 'mediocre' firms score below 50% on our framework. We rebalance these buckets once a year, taking into account the then rolling six years of financial data. The performance over the subsequent year is measured on a calendar year basis.

Exhibit 5: Average performance of Great, Good and Mediocre firms (2004-2013)



The BSE500 Index has returned 12.4% CAGR over this period whilst BSE500 ex-financials has delivered 11% over this period.

Source: Ambit capital research

Note that this back-test does not consider accounting or management quality, which we believe are factors that should improve the performance of our live portfolios.

Ten baggers 3.0

In the latest iteration of the ten-bagger exercise, from the 77 firms that clear more than two-thirds of our cut-off, we reach a shortlist of 30 firms, after following a process of elimination. This involves removing firms with poor scores on our accounting model (for a full exposition of our accounting filter, please refer to our [22 November 2013 note](#) which explains how our forensic accounting model works); firms with suspect corporate governance and firm with structural issues around the underlying business.

There are 12 changes (40% of the list) with respect to last year's list (refer to our [January 2013 note](#)). A summary of these changes is as follows:

- Exide, Jagran Prakashan, Sadbhav, Oberoi Realty, Balkrishna, CRISIL, Elgi Equipment, Nestle, Mahindra Life and Whirlpool drop out on account of deterioration in scores whilst Redington and Titan have been removed on account of forward-looking concerns.
- Bosch, eClerx, Kaveri Seeds, Page Inds, PI Industries, MRF, McLeod Russel, VST Industries, Tata Motors, Bajaj Auto, Castrol and DB Corp are the 12 names that are added using the FY13 data.

Having identified the 30 great firms that exhibit the ingredients required to be tomorrow's winners, we run a valuation check to ascertain if they are currently trading at reasonable prices for outright investments. In our view, whilst valuations do matter on a tactical basis, how the underlying fundamentals evolve for the firm over long periods plays a more important role in determining returns than the beginning of the period valuation itself. We discuss this in detail in the final section of this note.

Here, we categorise these stocks into three buckets based on their relative attractiveness on valuations with respect to their own history. We compare these firms with respect to their five-year average valuations on three metrics—P/B, P/E and EV/EBITDA. We find eight firms to be inexpensive (on at least two of the three metrics): Bajaj Auto, DB Corp, McLeod Russel, Torrent Power, Shoppers Stop, Cadila Healthcare, Cummins India and Tata Motors. However, for the long term, all 30 stocks remain candidates to be ten baggers from our perspective (as we have reiterated time and again that today's valuations do not have a significant effect on long-term returns! Please see page 14).

We have bottom-up coverage with BUYs on nine of these names: Cummins India, Supreme Industries, TTK Prestige, Eicher Motors, Torrent Power, Persistent Systems, eClerx Services, Tata Motors and Bajaj Auto.

An overlay of accounting and corporate governance checks to the greatness framework is the last but critical step.

For the long term, beginning valuations do not matter much.

Exhibit 6: November 2013 ten baggers - Valuation perspective

Sr. No.	Ticker	Company	Mcap (US\$ mn)	Trailing valuations			Cheap w.r.t history? (1 for "yes")			Overall cheap on how many counts?
				P/E	P/B	EV/EBITDA	P/E	P/B	EV/EBITDA	
Attractive valuations*										
1	BJAUT IN	Bajaj Auto	8,868	16.6	5.9	13	1	1	1	3
2	CDH IN	Cadila Health.	2,447	21.8	4.7	15.6	1	1	0	2
3	DBCL IN	D B Corp	771	17.7	4.1	10.5	1	1	1	3
4	KKC IN	Cummins India	1,891	17.5	4.7	15.7	1	1	0	2
5	MCLR IN	McLeod Russel	491	10.1	1.5	8	1	1	1	3
6	SHOP IN	Shoppers St.	438	136.3	5.4	27.2	0	1	1	2
7	TPW IN	Torrent Power	770	17.7	0.8	8	0	1	1	2
8	TTMT IN	Tata Motors	17,974	10.8	2.8	4.5	0	1	1	2
Moderate valuations**										
9	BOS IN	Bosch	4,300	27.6	4.5	18.6	0	1	0	1
10	BYRCS IN	Bayer Crop Sci.	1,019	21.5	3.2	14	0	1	0	1
11	CU IN	Carborundum Uni.	351	20.2	2	10.5	0	1	0	1
12	ITC IN	ITC	39,888	30.4	10.1	20.2	1	0	0	1
13	KSCL IN	Kaveri Seed Co.	349	14.6	5.4	10.3	0	0	1	1
14	LPC IN	Lupin	6,078	25.7	6.5	14.8	0	0	1	1
15	MRF IN	MRF	1,153	10.6	2.1	4.6	0	0	1	1
16	TTKPT IN	TTK Prestige	609	27.4	8	19.2	0	1	0	1
Rich valuations***										
17	APNT IN	Asian Paints	7,925	41.1	13.4	25	0	0	0	0
18	BATA IN	Bata India	1,087	36.4	8.9	22.3	0	0	0	0
19	CSTRL IN	Castrol India	2,289	30.6	20.8	20	0	0	0	0
20	ECLX IN	eClerx Services	536	16.2	6.7	10.6	0	0	0	0
21	EIM IN	Eicher Motors	1,829	31.6	5.8	16.5	0	0	0	0
22	IPCA IN	Ipca Labs.	1,379	22.4	5	13.3	0	0	0	0
23	KJC IN	Kajaria Ceramics	294	16.7	4.4	7.9	0	0	0	0
24	PAG IN	Page Industries	875	42.3	21.9	25	0	0	0	0
25	PI IN	P I Inds.	485	23.2	5	14.5	0	0	0	0
26	PSYS IN	Persistent Sys	567	15.3	3.1	8.4	0	0	0	0
27	SI IN	Supreme Inds.	798	16.5	5.2	9.6	0	0	0	0
28	SKB IN	GlaxoSmith C H L	2,958	39	12.5	27.5	0	0	0	0
29	TRP IN	Torrent Pharma.	1,237	16.3	4.8	10.3	0	0	0	0
30	VST IN	VST Inds.	390	18.8	8.1	11.8	0	0	0	0

Source: Bloomberg, Capitaline, Ambit Capital research.

* Trading below five-year average P/E, P/B, EV/EBITDA (on at least two of these three measures)

** Trading below either five-year average P/E, five-year P/B or five-year EV/EBITDA (on one of these three measures)

*** Trading above five-year average P/E, P/B and EV/EBITDA

Exhibit 7: November 2013 ten baggers' financial snapshot

Sr. No.	Bloom ticker	Company	Sector	Mcap (US\$ mn)	6M ADV (US\$ mn)	3-yr price CAGR	Net Sales (3-year CAGR)	Adj PAT (3-year CAGR)	CFO (3-year CAGR)	RoE (3-year avg)	RoCE (3-year avg)	PBIT margin (3-year avg)	Net Debt Equity (FY13)	FY14 P/E	FY14 P/B
Attractive valuations*															
1	BJAUT IN	Bajaj Auto	Auto	8,868	14	5%	20%	23%	-5%	58%	69%	18%	-0.7	15.4	4.9
2	CDH IN	Cadila Health.	Pharma	2,447	1.7	-1%	20%	8%	-5%	30%	24%	17%	0.8	20.5	4.2
3	DBCL IN	D B Corp	Media	771	0.3	1%	15%	6%	0%	27%	32%	23%	0	17	4.1
4	KKC IN	Cummins India	Capital Goods	1,891	2	-8%	17%	15%	-3%	31%	44%	17%	-0.4	19.5	4.5
5	MCLR IN	McLeod Russel	Agro	491	1.1	8%	15%	6%	-10%	17%	19%	23%	0.1	9	1.4
6	SHOP IN	Shoppers St.	Retail	438	0.3	-3%	30%	-43%	4%	4%	10%	3%	0.9	136.3	5.4
7	TPW IN	Torrent Power	Utilities	770	0.8	-29%	12%	-24%	-3%	18%	17%	20%	1.1	23	0.7
8	TTMT IN	Tata Motors	Auto	17,974	46.3	15%	27%	89%	35%	50%	24%	10%	0.6	9.2	2.4
Moderate valuations**															
9	BOS IN	Bosch	Auto Anc	4,300	0.6	10%	22%	18%	2%	21%	29%	13%	-0.5	27.2	4.2
10	BYRCS IN	Bayer Crop Sci.	Fertilizers	1,019	0.7	17%	16%	29%	19%	22%	30%	10%	-0.5	21.5	3.1
11	CU IN	Carborundum Uni.	Industrials	351	0	0%	15%	-4%	-1%	19%	20%	13%	0.3	15.9	1.9
12	ITC IN	ITC	FMCG	39,888	41.6	21%	18%	21%	17%	34%	50%	32%	-0.4	28.3	9.5
13	KSCL IN	Kaveri Seed Co.	Agro	349	0.5	61%	64%	63%	75%	32%	31%	18%	-0.4	12.3	4.4
14	LPC IN	Lupin	Pharma	6,078	14.7	20%	26%	25%	23%	28%	27%	18%	0.1	22.6	5.7
15	MRF IN	MRF	Auto Anc	1,153	3.5	26%	28%	33%	7%	21%	21%	7%	0.4	8.5	1.6
16	TTKPT IN	TTK Prestige	Consumer Durable	609	1.7	29%	39%	39%	16%	47%	62%	15%	0.2	26.7	6.5
Rich valuations***															
17	APNT IN	Asian Paints	FMCG	7,925	9.1	25%	18%	12%	4%	39%	52%	15%	-0.2	37.9	12.2
18	BATA IN	Bata India	Retail	1,087	4.7	44%	19%	40%	23%	28%	48%	12%	-0.3	33.9	8
19	CSTRL IN	Castrol India	Chemicals	2,289	0.7	9%	10%	5%	-6%	83%	124%	22%	-0.9	29.4	19.6
20	ECLX IN	eClerx Services	IT	536	0.6	17%	37%	33%	36%	53%	60%	35%	-0.6	13.3	5.7
21	EIM IN	Eicher Motors	Auto	1,829	1.6	54%	30%	53%	9%	18%	26%	8%	-0.8	28.2	5.2
22	IPCA IN	Ipca Labs.	Pharma	1,379	2.3	29%	21%	16%	27%	25%	24%	15%	0.4	18	4.4
23	KJC IN	Kajaria Ceramics	Miscellaneous	294	0.5	47%	30%	43%	-4%	32%	29%	13%	0.9	15.9	3.7
24	PAG IN	Page Industries	Retail	875	0.6	51%	36%	42%	43%	58%	57%	19%	0.4	35.9	18.2
25	PI IN	P I Inds.	Fertilizers	485	0.3	62%	28%	32%	5%	29%	26%	13%	0.4	17.5	4.4
26	PSYS IN	Persistent Sys	IT	567	0.6	31%	29%	18%	20%	19%	23%	16%	-0.4	14.7	3
27	SI IN	Supreme Inds.	Industrials	798	0.4	38%	19%	24%	41%	39%	38%	13%	0.5	15.7	4.7
28	SKB IN	GlaxoSmith C H L	FMCG	2,958	2.4	24%	18%	23%	11%	34%	51%	16%	-1.1	35.7	11.5
29	TRP IN	Torrent Pharma.	Pharma	1,237	0.8	18%	19%	27%	-19%	31%	28%	16%	0	14.7	4.1
30	VST IN	VST Inds.	FMCG	390	0.2	36%	12%	25%	31%	41%	63%	24%	-0.8	17.6	7.9

Source: Bloomberg, Ambit Capital research

Exhibit 8: November 2013 ten baggers - Forward-looking data using consensus estimates

Sr. No.	Ticker	Company	Mcap (US\$ mn)	6-month ADV (US\$ mn)	Next 3 years' estimated EPS CAGR	Next 3 years' estimated BVPS CAGR
1	APNT IN	Asian Paints	7,925	9.1	16%	18%
2	BATA IN	Bata India	1,087	4.7	17%	20%
3	BJAUT IN	Bajaj Auto	8,868	14	15%	23%
4	BOS IN	Bosch	4,300	0.6	10%	16%
5	BYRCS IN	Bayer Crop Sci.	1,019	0.7	24%	28%
6	CDH IN	Cadila Health.	2,447	1.7	22%	18%
7	CSTRL IN	Castrol India	2,289	0.7	6%	2%*
8	CU IN	Carborundum Uni.	351	0	32%	12%
9	DBCL IN	D B Corp	771	0.3	21%	15%
10	ECLX IN	eClerx Services	536	0.6	21%	36%
11	EIM IN	Eicher Motors	1,829	1.6	29%	20%
12	IPCA IN	Ipca Labs.	1,379	2.3	23%	24%
13	ITC IN	ITC	39,888	41.6	17%	12%
14	KJC IN	Kajaria Ceramics	294	0.5	24%	32%
15	KKC IN	Cummins India	1,891	2	3%	11%
16	KSCL IN	Kaveri Seed Co.	349	0.5	23%*	35%*
17	LPC IN	Lupin	6,078	14.7	25%	28%
18	MCLR IN	McLeod Russel	491	1.1	12%	13%
19	MRF IN	MRF	1,153	3.5	7%*	23%*
20	PAG IN	Page Industries	875	0.6	33%*	36%*
21	PI IN	P I Inds.	485	0.3	23%	31%
22	PSYS IN	Persistent Sys	567	0.6	18%	18%
23	SHOP IN	Shoppers St.	438	0.3	NA	3%*
24	SI IN	Supreme Inds.	798	0.4	18%	22%
25	SKB IN	GlaxoSmith C H L	2,958	2.4	16%	17%
26	TPW IN	Torrent Power	770	0.8	27%	10%
27	TRP IN	Torrent Pharma.	1,237	0.8	21%	22%
28	TTKPT IN	TTK Prestige	609	1.7	18%	29%
29	TTMT IN	Tata Motors	17,974	46.3	23%	26%
30	VST IN	VST Inds.	390	0.2	6%	5%*

Source: Bloomberg, Ambit Capital research; Note: * indicates next two-year CAGR

Greatness framework on sub-BSE500 firms

Last year, based on client feedback, we had inserted a list of sub-BSE500 firms that did well on our framework primarily in the hope that running the screen on relatively lesser known names should work even better. The results surely have been very encouraging. The sub-BSE500 list from last year delivered 22.4% in absolute terms and 41.2% relative to the BSE Smallcap Index (please see page 13 for performance details).

Continuing with this initiative, we present below a list of select smallcaps from outside the BSE500 but above a market cap of Rs3,500mn that fare well on this year's iteration of our greatness framework (after updating FY13 numbers). However, since our forensic accounting model has been built only for the BSE500 universe, the list below has not been filtered for suspect accounting or suspect corporate governance.

The framework should work better in the less-discovered sub-BSE500 universe.

Exhibit 9: November 2013 greatness framework on smaller caps outside BSE500 (without filtering for suspect accounting or corporate governance)

Sr. No.	Ticker	Company	Mcap (US\$ mn)	6-month ADV (US\$ mn)	FY14 P/E (est)	FY14 P/B (est)
1	MUNI IN	Mayur Uniquote	117	0.0	14.1	4.5
2	SEL IN	Suprajit Engineering	76	0.0	9.8	2.3
3	PLM IN	Poly Medicure	120	0.1	NA	NA
4	GWN IN	Grindwell Norton	226	0.0	10.1	NA
5	ASTM IN	Astra Microwave	60	0.1	8.4	1.6
6	SDB IN	Som Distilleries	133	0.1	NA	NA
7	HTSMF IN	Hatsun Agro Products	342	0.0	39.2	11.6
8	SPPT IN	Supreme Petrochem	91	0.0	5.1	1.1
9	LOG IN	La Opala RG	95	0.2	20.1	5.9
10	SVLS IN	Suven Life Sciences	135	0.9	17.1	4.1
11	ASTRA IN	Astral Poly	225	0.2	18.2	4.4
12	WHL IN	Wheels India	119	0.4	NA	NA
13	HMVL IN	Hindustan Media	128	0.0	7.8	1.3
14	KALE IN	Accelya Kale	146	0.2	8.7	5.7
15	CRS IN	Cera Sanitary.	120	0.1	14.2	3.3
16	KEKC IN	Kewal Kiran Clothing	219	0.1	20.6	4.7

Source: Ambit Capital research, Note: NA indicates Data Not Available

Performance check: Jan 2013 ten-bagger list

Exhibit 10: The ten-bagger list published on 14 January 2013

		M Cap (US\$ mn)	Price		Performance
			11-Jan-13	25-Nov-13	
Attractive Valuations*					
CU IN Equity	Carborundum Uni.	504	146	117	-20%
EXID IN Equity	Exide Inds.	2,236	141	111	-21%
JAGP IN Equity	Jagran Prakashan	659	113	81	-28%
MLIFE IN Equity	Mahindra Life.	303	394	393	0%
REDI IN Equity	Redington India	635	85	68	-20%
SADE IN Equity	Sadbhav Engg.	373	133	76	-43%
TPW IN Equity	Torrent Power	1,553	177	102	-43%
TTAN IN Equity	Titan Inds.	4,338	270	228	-15%
Average for this bucket					-24%
Moderate Valuations**					
BATA IN Equity	Bata India	1,029	855	1053	23%
NEST IN Equity	Nestle India	8,573	4840	5436	12%
OBER IN Equity	Oberoi Realty	1,704	271	192	-29%
PSYS IN Equity	Persistent Sys	385	541	889	64%
SHOP IN Equity	Shoppers Stop	670	433	330	-24%
WHIRL IN Equity	Whirlpool India	643	281	163	-42%
Average for this bucket					1%
Rich Valuations***					
APNT IN Equity	Asian Paints	7,659	430	516	20%
BIL IN Equity	Balkrishna Inds	533	299	285	-4%
BYRCS IN Equity	Bayer Crop Sci.	891	1212	1630	34%
CDH IN Equity	Cadila Health.	3,248	860	743	-14%
CRISIL IN Equity	CRISIL	1,325	1015	1054	4%
EIM IN Equity	Eicher Motors	1,387	2811	4203	50%
ELEQ IN Equity	Elgi Equipment	281	94	82	-13%
IPCA IN Equity	Ipca Labs.	1,156	488	685	40%
ITC IN Equity	ITC	40,518	273	316	16%
KJC IN Equity	Kajaria Ceramics	315	233	249	7%
KKC IN Equity	Cummins India	2,640	516	427	-17%
LPC IN Equity	Lupin	4,791	588	851	45%
SI IN Equity	Supreme Inds.	717	303	394	30%
SKB IN Equity	GlaxoSmith C H L	2,978	3863	4401	14%
TRP IN Equity	Torrent Pharma.	1,160	374	462	23%
TTKPT IN Equity	TTK Prestige	749	3532	3290	-7%
Average for this bucket					14%
Overall Average					1.4%
BSE500 Index			7641	7522	-1.6%
Outperformance					3.0%

Source: Bloomberg, Ambit Capital research

On average, last year's iteration of ten baggers published on 14 January 2013 have clocked nearly 1.4% returns in absolute terms and 3% relative to the BSE500 over the year. This compares with an absolute return of 29.4% and a relative return (to BSE500) of 6.7% delivered by the first iteration. Moreover, the beginning-of-the-period valuations have not made much difference to returns as seen from the performance of the three valuation buckets.

Performance check: Jan 2013's sub-BSE500 firms

Exhibit 11: Superior firms on 'greatness' from sub-BSE500 published on 14 January 2013

		Price		Performance
		11-Jan-13	25-Nov-13	
VO IN Equity	Vinati Organics	152	171	12%
HMVL IN Equity	Hindustan Media	155	109	-30%
MUNI IN Equity	Mayur Uniquote	243	339	40%
ICSL IN Equity	Infinite Comp	129	128	0%
CLRC IN Equity	Clariant Chemical	618	584	-5%
PI IN Equity	P I Inds.	134	221	65%
HAWK IN Equity	Hawkins Cookers	2,408	2,175	-10%
ZENT IN Equity	Zensar Tech.	277	333	20%
AJP IN Equity	Ajanta Pharma	264	1,004	280%
GDYR IN Equity	Goodyear India	333	361	8%
SWE IN Equity	Swaraj Engines	499	609	22%
CRS IN Equity	Cera Sanitary.	423	594	40%
SEQ IN Equity	Sequent Scien.	217	140	-35%
KEKC IN Equity	Kewal Kir.Cloth.	726	1,111	53%
SRL IN Equity	Speciality Rest.	178	112	-37%
STAL IN Equity	Styrolution ABS	722	400	-45%
FMGI IN Equity	Federal-Mogul	192	195	2%
Overall average				22.4%
BSE Smallcap Index		7,455	6,053	-18.8%
Outperformance				41.2%

Source: Bloomberg, Ambit Capital research

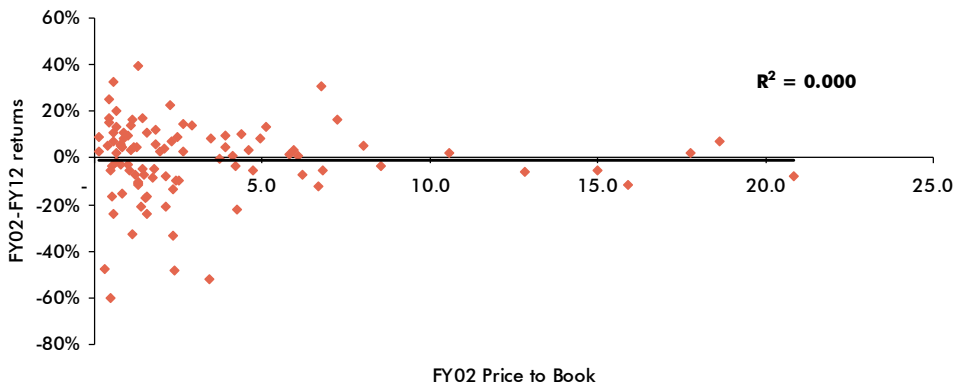
The sub-BSE500 list of firms published on 14 January 2013 has shown a stellar performance over the year. These stocks are up 22% on average over the year whilst they have outperformed the BSE Smallcap Index by a whopping 41% since publication. Even after excluding Ajanta Pharma, the superstar performer, the outperformance is still a handsome 25.1%, suggesting that the framework does a good job in the sub-BSE500 universe.

Valuations - A long-term perspective!

We have published research over the past few months indicating how 'quality at a reasonable price' should be the best way of playing India tactically at this juncture given the extreme valuation polarisation today. Thus, we do acknowledge that from a tactical standpoint valuations play an important role in shaping short-term returns.

However, over long periods, it is how the underlying fundamentals evolve for the firm that plays a more important role in determining returns than the beginning of the period valuation itself. This point can be understood better with the following exhibits that plot ten-year returns over FY02-12 vs FY02 valuations as measured by P/B and P/E at the beginning of the period (in 2002).

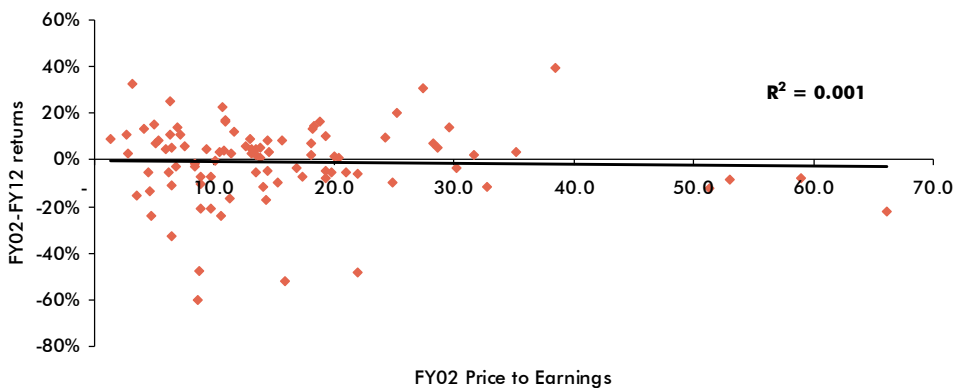
Exhibit 12: Valuation impact on long-term returns - P/B



Source: Ambit Capital research; Note: FY02 – FY12 returns here are stock returns relative to Sensex

The value of R-square makes the story self-explanatory. A zero for this value indicates that the beginning-of-period valuations do not play any meaningful role in explaining stock returns over the next ten years. This holds true for both P/B and P/E as the measures of valuation.

Exhibit 13: Valuation impact on long-term returns - P/E



Source: Ambit Capital research; Note: FY02 – FY12 returns here are stock returns relative to Sensex

Thus, even with a preference for 'quality at a reasonable price' approach, as reflected in our latest Good & Clean portfolio (G&C 6.1), the two exhibits above clearly suggest that from a long-term perspective each of these stocks stand a fair chance of delivering superior shareholder returns. Indeed, as reflected in the performance of the portfolio on page 10, the beginning-of-period valuations and the returns generated over the subsequent 12 months do not have any correlation so far.

Appendix - Nov 2013 ten-baggers' business activity description

Sr. No.	Ticker	Company	Business Description
1	CU IN	Carborundum Uni.	Carborundum Universal manufactures refractories and electromineral grains. The company produces coated and bonded abrasives, super refractories, aluminum oxide grains, calcined bauxite, electrocast refractories, silicon carbide grains and industrial ceramic products.
2	TPW IN	Torrent Power	Torrent Power Limited generates, transmits and distributes power. The company also implements large power projects in India.
3	BATA IN	Bata India	Bata India Limited manufactures a wide range of leather, rubber/canvas and plastic footwear products. The company also manufactures sports apparel and leather accessories. Bata India sells its products through its chain of company-owned retail stores in India, as well as to businesses in the US, the UK, Europe, the Middle East and the Far East.
4	PSYS IN	Persistent Sys	Persistent Systems Limited offers outsourced software product development. The company offer services that include testing, support, and professional services.
5	SHOP IN	Shoppers St.	Shoppers Stop Ltd operates a chain of retail shops. The company retails men's, women's, and children's clothing, cosmetics and skin and hair care products, home appliances, housewares, linens, luggage, jewelry, and accessories.
6	APNT IN	Asian Paints	Asian Paints Limited manufactures a wide range of decorative paints, varnishes, enamels, and black & synthetic resins. The company, through its subsidiaries, also manufactures specialty industrial chemicals and vinyl pyridine latex products which are used in the manufacture of rubber tires.
7	BYRCS IN	Bayer Crop Sci.	Bayer Cropscience Ltd. is involved in crop science in the area of crop protection, non agricultural pest-control, seeds and plant biotechnology.
8	CDH IN	Cadila Health.	Cadila Healthcare Ltd. manufactures and markets healthcare solutions ranging from formulations, active pharmaceutical ingredients, vaccines, diagnostics, health and dietetic foods, animal healthcare to cosmeceuticals. The company's products are available in tablets, capsules, injections, liquids, dry syrups, powders, granules, and ointments.
9	EIM IN	Eicher Motors	Eicher Motors Ltd. manufactures light commercial vehicles which are sold domestically and are also exported to other countries. Eicher Motors also manufactures tractors, two-wheelers and automotive gears.
10	IPCA IN	Ipca Labs.	Ipca Laboratories Limited operates a pharmaceutical company, which distributes products to over 75 countries worldwide. The Group's products include finished dosage forms, drug delivery systems, bulk drugs and intermediates.
11	ITC IN	ITC	ITC Limited, a member of the BAT Group of the UK, is a holding company which has a diversified presence in cigarettes, hotels, paperboards & specialty papers, packaging, agri business, packaged foods & confectionery, branded apparel, greeting cards and other FMCG products.
12	KJC IN	Kajaria Ceramics	Kajaria Ceramics Limited manufactures glazed and unglazed ceramic tiles. The company sells its products in India and it also exports them to other countries.
13	KKC IN	Cummins India	Cummins India Limited manufactures internal combustion engines, including diesel, reciprocating piston, gas turbine and gasoline engines. The company also manufactures generating sets and public transport-type passenger motor vehicles, including luxury coaches and air-field buses. In addition, Cummins India Ltd. operates a computerised and fully-equipped research and development facility.
14	LPC IN	Lupin	Lupin Limited manufactures bulk actives and formulations. The principal bulk actives manufactured by it include Rifampicin, Pyrazinamide, Ethambutol (anti-TB), Cephalosporins (anti-infectives) and cardiovasculars. The company also possesses competencies in phytomedicines, in which medicines are made out of plant and herbal resources supported by the discipline of modern medicine.
15	SI IN	Supreme Inds.	Supreme Industries Limited manufactures industrial and engineered molded products and storage and material handling crates. The company also manufactures chemicals, multi-layer sheets, multi-layer films, packaging films and expanded polyethylene foam, PVC pipes and fittings, molded furniture and disposable EPS containers.
16	SKB IN	GlaxoSmith C H L	Glaxo SmithKline Consumer Healthcare Limited manufactures and sells malted milk food products. The Group's products, which include energy & protein products, cereals, baby foods, ghee & butter, are sold under the "Horlicks", "Boost", "Viva", "Brylcream", "E-no", "Maltova" and "Gopika" brand names.
17	TRP IN	Torrent Pharma.	Torrent Pharmaceuticals Ltd. manufactures bulk drugs and pharmaceutical formulations. The company's formulations include cardio-vascular, psychotropic and anti-biotic drugs while its bulk drugs include atenolol, ciprofloxacin and norfloxacin. Torrent Pharmaceuticals has wholly owned subsidiaries in several regulated and less-regulated international markets.
18	TTKPT IN	TTK Prestige	TTK Prestige Limited manufactures a range of domestic appliances. The Group's products include pressure cookers and non-stick cookware, stainless steel and glass vacuum flasks, and gas stoves.
19	BOS IN	Bosch	Bosch Limited manufactures a wide range of automotive parts. The company's products include fuel injection pumps, spark plugs, including nozzles and nozzle holders, elements, delivery valves, filters and filter inserts, glow plugs, starter motors, alternators and wipers. Bosch also manufactures hydraulic and pneumatic equipment and electric power tools and fixtures.
20	ECLX IN	eClerx Services	eClerx Services Limited provides data analytics and solutions to global enterprise clients in the financial services, retail and manufacturing industries. The company offers data analytics, operations management, data audits, metrics management and reporting services.
21	KSCL IN	Kaveri Seed Co.	Kaveri Seed Co Limited produces, processes, and markets hybrid seeds for crops that include corn, sunflower, cotton, paddy, and grain.
22	PAG IN	Page Industries	Page Industries Limited develops, produces, and distributes branded underwear for men, women, and children in India and Sri Lanka.
23	PI IN	P I Inds.	PI Industries Limited manufactures agricultural and fine chemicals, and polymers. The company produces fine chemicals, crop protection, plant nutrients, and seeds, and engineering plastics for use in the automobile, electrical, and home appliances industries.

Sr. No.	Ticker	Company	Business Description
24	MRF IN	MRF	MRF Limited manufactures and distributes tyres and tubes for automobiles, aircrafts, motorcycles and cycles. The company also manufactures conveyor belts, paint and coats, and hoses. Every MRF tyre designed is the result of a special acid test on the race and rally tracks.
25	MCLR IN	McLeod Russel	McLeod Russel India Ltd. cultivates, manufactures, and markets tea. The Group owns tea estates in Assam and Dooars.
26	VST IN	VST Inds.	VST Industries Ltd. manufactures and distributes cigarettes and tobacco products. The company's cigarette brands include "Charminar Specials," "Shah-I- Deccan," "Charms Virginia Filter Kings," "Vazir," "Qila" and "Ambassador." VST Industries sells its products in India and abroad.
27	TTMT IN	Tata Motors	Tata Motors Limited manufactures cars and commercial automotive vehicles in India. The company designs, manufactures and sells heavy commercial, medium commercial and small commercial vehicles including trucks, tankers, vans, buses, ambulances and minibuses. Tata also manufactures small cars and sports utility vehicles.
28	BJAUT IN	Bajaj Auto	Bajaj Auto Limited manufactures and distributes motorised two-wheeled and three-wheeled scooters, motorcycles and mopeds.
29	CSTRL IN	Castrol India	Castrol (India) Limited manufactures and markets automotive and industrial lubricants and specialty products. The company's products include lubricating oils, greases and brake fluids. The company also manufactures cable filling compounds, jellies, waxes and other items.
30	DBCL IN	D B Corp	DB Corporation Ltd. is a print media and publishing company.

Source: Bloomberg

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Explanation of Investment Rating

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